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THE GOVERNANCE OF FOREIGN INVESTMENT AT A CROSSROAD: IS AN OVERLAPPING CONSENSUS  
THE WAY FORWARD?

Nicolás M. Perrone\*

This article makes the claim that the present efforts to reform the international investment regime will not save this field from the existing criticism. Given the plural values at issue, it is unlikely that states—let alone local populations—will ever reach a consensus on the substantive questions surrounding foreign investment. Historically, the main characteristic of foreign investment governance has in fact been the lack of multilateral consensus. This field remained dominated by diplomacy and customary international law until bilateral treaties and investment arbitration consolidated as the leading mechanism to resolve investment disputes in the 1990s. This highly legalised regime, however, has been subject to criticism from developing and now increasingly from developed countries. Most reform proposals yet fail to go beyond alternatives that have been unsuccessful in the past, such a multilateral investment agreement or state-to-state arbitration. This article takes a different approach to foreign investment governance starting from its political economy. It claims that the international investment regime does not depoliticise foreign investment relations but rather promotes the politics of foreign investors' private property protection. Relying on property theory and pluralism as heuristic tools, this article analyses the resistance to investment arbitration, the obstacles to multilateral cooperation, and the possibility of an overlapping consensus on the basic institutions to govern foreign investment.

What is at issue is the degree of freedom that should be allowed the multinational corporation or the nature and extent of regulation that should be imposed on its present operations and future growth in order to make it better serve divergent national interests.

U.S. Department of Commerce, 1973<sup>1</sup>

## ***I. Introduction***

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<sup>1</sup> U.S. Department of Commerce, "The Multinational Corporation—An Overview," in *Multinational Corporations*, a compendium of papers published by the U.S. Senate Committee on Finance, 21 February, 1973, p. 42.

The mismatch between the global corporate reality and national political authorities is a central issue in economic regulation. Multinational corporations (MNCs) are active in different countries and view the world as a single market to do business. They are involved in the production of natural resources, outsource many of their activities, and sell final products globally. National political authorities may attempt to regulate any of these activities for a public purpose. But they are unable to tackle the entire business structure or the global value chain. This can create two kinds of political tensions. On the one hand, there is a potential problem of distribution of benefits between MNCs and the different host states. An area where this is clear is international taxation, where MNCs can rely on different tax planning tools such as transfer pricing. On the other hand, there is a constant tension between the global and local perspective. What local communities expect of foreign economic activities may be quite different from a maximum effective utilization of economic resources.

This mismatch between economic activity and political authority has attracted much attention from governments as well as the literature in international relations, international law and international economics.<sup>2</sup> In 1969, the U.S. Assistant Secretary of State for Economic Affairs predicted that the “problems of conflicting jurisdictions and of regulation in the public interest will [...] lead inevitably to international agreement and perhaps to international machinery for administration.”<sup>3</sup> But despite the large academic and governmental interest, there has been a systemic lack of multilateral consensus on the governance of foreign investment. Most governance initiatives of MNC activity today are based on voluntary corporate social responsibility initiatives.<sup>4</sup>

The situation of MNCs, paradoxically, has attracted much less attention. State activity nonetheless can undermine foreign investors’ use of resources if each country follows a particular regulatory philosophy aimed at materialising social goals as different as economic growth and community welfare. What is interesting is that while there is little regulation for MNCs at a global scale, there are several international legal tools in place that MNCs can use to supervise and discipline state activity. The international business lobby demanded and obtained the establishment of international mechanisms for the protection of foreign investment, while

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<sup>2</sup> Rehinder, Eckard, “The Foreign Direct Investment Regulations: A European Legal Point of View,” *Law and Contemporary Problems* 34.1 (1969): 95-117; Vagts, Detlev “The multinational enterprise: A new challenge for transnational law,” *Harvard Law Review* (1970): 739-792.

<sup>3</sup> Solomon, Anthony, “Foreign Investment Controls: Policy and Response,” *Law and Contemporary Problems* 34.1 (1969), p. 125.

<sup>4</sup> The most important of these initiatives is the U.N. Global Compact. See [www.unglobalcompact.org/](http://www.unglobalcompact.org/).

convincing states that social and environmental issues should remain regulated at a domestic level.<sup>5</sup>

The paradigm of these mechanisms is investment arbitration, a dispute resolution mechanism for foreign investment disputes that operates according to international treaties for the protection of foreign investment. Most of these treaties are bilateral (BITs) and deal only with protection, although this tendency is changing and foreign investment liberalisation is being introduced in recent free trade agreements. Presently, the network of investment treaties includes more than 3,000 agreements.<sup>6</sup> The literature concurs that these treaties, despite some differences between them, constitute a regime with common “principles, norms, rules and decision making procedures.”<sup>7</sup> The relevance acquired by the international investment regime (IIR) in the last two decades is mainly a result of investment arbitration. Investment treaties empower MNCs to sue host states directly before international arbitral tribunals, without exhausting local remedies or requesting the espousal of their home states. These tribunals are empowered to review the behaviour of the host state, considering whether it breached the standards of protection incorporated in the applicable treaty.

It is possible to characterise the IIR within the trend of private international empowerment *vis-à-vis* national states. Investment treaties impose obligations to every signatory country, and these obligations only refer to standards of foreign investment protection. Since the inception of the IIR, however, developed countries only identified themselves with the role of home states.<sup>8</sup> Large corporations based on their territories and owned by national individuals were competing for raw materials and markets in the new postcolonial world. These investors needed security against the political authority of newly independent countries. Signing investment treaties was a way to facilitate the calculability of western business in foreign countries. Since developing countries were not expecting a sudden outflow of capital towards the developed world,

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<sup>5</sup> Stiglitz, Joseph, “Regulating Multinational Corporations: Towards Principles of Cross-Border Legal Framework in a Globalized World. Balancing Rights with Responsibilities,” *American University International Law Review* 23 (2007), pp. 466-469; Levy, David and Aseem Prakash, “Bargains old and new: Multinational corporations in global governance,” *Business and Politics* 5.2 (2003): 131-150.

<sup>6</sup> UNCTAD, *World Investment Report 2013: Global Value Chains: Investment and Trade for Development* (New York and Geneva: United Nations, 2013), p. xix.

<sup>7</sup> Salacuse, Jeswald, “The Emerging Global Regime for Investment,” *Harvard International Law Journal* 51 (2010), p. 431; Schneiderman, David, *Constitutionalizing Economic Globalization. Investment Rules and Democracy’s Promise* (New York: Cambridge University Press, 2008), p. 26.

<sup>8</sup> Miles, Kate *The origins of international investment law: empire, environment, and the safeguarding of capital* (Cambridge: Cambridge University Press, 2013), pp. 2-3; Sornarajah, M., “Power and justice in foreign investment arbitration,” *Journal of International Arbitration* 14.3 (1997): 103-140.

investment treaties represented an asymmetric consensus that was “one-sidedly extended to developing countries.”<sup>9</sup>

The asymmetric structure of the IIR began to change only recently when developed states had to appear before investment tribunals as *respondents*. According to UNCTAD, 27% of the investment arbitrations in 2013 were initiated against developed states.<sup>10</sup> This is a result of two central developments. First, MNCs are not coming any longer from western developed countries only but from China, Brazil, India, Russia and several other nations. This new political economy breaks the *de facto* asymmetry of the regime, as China for instance has rapidly developed a new investment treaty program.<sup>11</sup> Second, the international business lobby has pushed the IIR structure beyond its original postcolonial roots, i.e. beyond the original asymmetric character. After the creation of NAFTA, it became clear that investment arbitration not only served for Canadian and U.S. American corporations to sue Mexico, but also for these foreign investors to sue the United States and Canada.<sup>12</sup>

As the asymmetric structure of the IIR fades, this article will argue that the original consensus for the proliferation of investment treaties may come to an end too. While the international business and legal lobby continues to push for investment arbitration in every possible economic deal, governments and civil societies no longer only from Ecuador, Venezuela or Bolivia but now also from Australia, France and Germany begin to reconsider this regime, or at least, to reconsider whether they want to continue moving towards a universal model of investment protection.<sup>13</sup> Many actors in developed states did not worry about investment arbitration until very recently because this mechanism was meant to facilitate corporate control of resources in other latitudes; it was a problem of others. But as the *North v. South* dynamic of foreign investment changes, actors in the developed world are beginning to think about the IIR in *Private v. Public* terms: a side of the struggle that has concerned developing countries for many years.

The generalisation of the resistance and discontent about the IIR is a recent phenomenon, and may be indicating the decay of this regime or, at least, an increasing space for contestation and

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<sup>9</sup> Andersson, Thomas, *Multinational investment in developing countries: a study of taxation and nationalization* (New York: Routledge, 1991), p. 11.

<sup>10</sup> UNCTAD, “Recent Developments in Investor-State Dispute Settlement (ISDS),” IIA Issues Note 1, April 2014, p. 7.

<sup>11</sup> Gallagher, Norah and Wenhua Shan, *Chinese investment treaties: policies and practice* (New York: Oxford University Press, 2009).

<sup>12</sup> For the cases files against the United States, see <http://www.state.gov/s/l/c3741.htm>. For the cases filed against Canada, see <http://www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/gov.aspx?lang=eng>.

<sup>13</sup> See Jandhyala, Srividya; Witold J. Henisz and Edward D. Mansfield, “Three Waves of BITs: The Global Diffusion of Foreign Investment Policy,” *Journal of Conflict Resolution* 55.6: 1047-1073.

change.<sup>14</sup> Back are the days of the alleged *de facto* multilateral consensus. The IIR thus faces three potential scenarios. It can overcome the legitimacy crisis, continuing the path envisioned by Wälde towards a universal regime applicable to every investor; it can gradually recover its asymmetric structure; or it can evolve into a broader institutional framework for the governance of foreign investment. This opportunity to reconsider foreign investment governance should not be taken lightly. It is one of the few international economic fields where multilateral consensus has remained impossible, and it is difficult to think of MNCs as regulated citizens of the world without such a multilateral consensus.

Rather than engaging in futurology, the objective of this article is to contribute to understanding the resistance to the IIR, the obstacles to multilateral cooperation in foreign investment affairs, and the realistic space for an overlapping consensus for the governance of MNCs. Presently, there are new calls for a multilateral investment regime or for increasing the engagement of states in investment litigation. These proposals focus on the consolidation of the present structure of the IIR, considering some minor reforms to improve this regime.<sup>15</sup> None of them, however, begins the analysis with the political economy of foreign investment or the purpose that an international regime should pursue. The objective of this article is to start exactly at this point, emphasising the relational implications of foreign investment.<sup>16</sup> My main argument is that the IIR empties foreign investment governance from most political content and purpose except for one particular goal: the facilitation of multinational corporate use and benefit of resources. This affects any competing local view on the disputes with MNCs. Defenders of the IIR claim that the advantage of investment arbitration is the “depolitisation” of foreign investment relations.<sup>17</sup> By this they mean the reduction of home and host state political interference in the enforcement of allegedly clear government commitments.<sup>18</sup> As I will show, however, the IIR does not eliminate politics but rather consolidates a particular kind of politics: the politics of foreign investors’ private property protection.

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<sup>14</sup> UNCTAD, “Reform of the IIA Regime: Four paths of action and a way forward,” IIA Issue Note 3, June 2014.

<sup>15</sup> Åslund, Anders, “The World Needs a Multilateral Investment Agreement,” Peterson Institute for International Economics PB 13-01 (2013); Graugnard, Nicole, “Toward a multilateral framework for investment,” Columbia FDI Perspectives 103 (2013); Hufbauer, Gary and Sherry Stephenson, “The case for a framework agreement on investment,” Columbia FDI Perspectives 116 (2013); Roberts, Anthea, “State-to-State Investment Treaty Arbitration: A Hybrid Theory of Interdependent Rights and Shared Interpretive Authority,” *Harvard International Law Journal* 55.1 (2014): 1-70.

<sup>16</sup> Kennedy, David, “The Mystery of Global Governance,” in Jeffrey Dunoff and Joel Trachtman, *Ruling the world?: constitutionalism, international law, and global governance* (New York : Cambridge University Press, 2009), p. 77.

<sup>17</sup> Broches, Aron, “Settlement of Investment Disputes,” in Aron Broches, *Selected Essays: World Bank, ICSID and Other Subjects of Public and Private International Law* (Dordrecht: Martinus Nijhoff Publishers, 1995), pp. 161, 163; Shihata, Ibrahim, “Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA,” *ICSID Review – Foreign Investment Law Journal* 1.1 (1986): 1-25.

<sup>18</sup> Elkins, Zachary, Andrew Guzman and Beth Simmons, “Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000,” *International Organization* 60 (2006), p. 834.

The second section of this article will describe the governance conundrum of foreign investment. It will show that the activity of multinational corporations brings about very delicate issues for host countries and populations and that these issues have most in common with the problems that private property rights create at the domestic level in terms of both state authority and democracy. The third section will make a historical analysis of the long record of multilateral disagreements on foreign investment. This will serve as the starting point to consider the structure and politics of the IIR. The fourth section will rely on the late Rawls to consider the possibility of reaching an overlapping consensus on the basic political institutions to govern the problems created by MNCs. This approach can coexist with a plurality of equally valid ideas on property and the use of resources. This section will illustrate some of the challenges for this strategy looking at the World Trade Organisation (WTO). The article will conclude by stressing that the IIR puts local populations in a state of vulnerability *vis-à-vis* foreign investors, promoting anxiety and distrust among states and civil society. It will suggest that a broader institutional structure can help politics recover its necessary place in the governance of foreign investment.

## ***II. The political economy of foreign investment: A question of private property and foreign ownership***

Most of the contentious issues that foreign investment creates relate to the control of resources in host countries, including natural resources, infrastructure and means of production. Many countries have natural resources and some of the necessary conditions to develop their economies. They lack, however, the capital and technology to use those resources. When the issue is put in these terms, the solution seems quite straightforward: bring the capital and the technology from abroad. This solution, however, does come with a cost: “Private investors invest to make profits and not for reasons of benevolence.”<sup>19</sup> MNCs are only likely to invest in a country when there is a prospect of profitability and they can ensure the control of the key resources comprising the investments. Private property rights are essential for any business plan because they legally transfer the control of the resources from host states or local individuals to foreign investors. A private property system is—as Lipson remarks—a necessary step to tap foreign investors’ energies.<sup>20</sup> In this regard, if the expansion of foreign private investment is to be

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<sup>19</sup> Akinsanya, Adeoye, “International Protection of Direct Foreign Investments in the Third World,” *The International and Comparative Law Quarterly* 36 (1987), p. 58.

<sup>20</sup> Lipson, Charles, *Standing Guard: Protecting Foreign Capital in the Nineteenth and Twentieth Centuries* (Berkeley: University of California Press, 1985), pp. 8-19.

equated with the development of capitalism beyond national borders, institutional economics unanimously anticipates the centrality of the internationalisation of private property rights.<sup>21</sup>

The problems that foreign investment creates in host countries are analytically similar to those created by the private ownership of resources. The conflict between foreign investors, host states and local population is not considerably different when the investors are domestic.<sup>22</sup> This does not mean that the foreign character of an investor can be ignored because, in fact, it often tends to exacerbate the problems created by private property.<sup>23</sup> But the bases to consider the political economy of foreign investment should be those of private property, properly complemented with the relevance of the foreign elements, including the role of home states.

Private property is always in tension with sovereignty and democracy. This tension is caused by the authority that property rights vest on the owners of resources, in particular of key and strategic resources.<sup>24</sup> Property rules govern the relation between individuals regarding the use and benefit of resources, and these rules are good against the entire world. Private property grants the owner the authority not only to use and benefit from the resources, i.e. to control them, but also to exclude other individuals and the state from interfering with this use. According to legal realism, the right to exclude represents the coercion that property rules impose on the rest of the social actors, whether private or public.<sup>25</sup> In this line of argument, granting property rights to foreign investors implies a passive obligation for the state not to interfere with the foreign investor's use of the resources, and an active obligation to police any individual who interferes with that use without the consent of the foreign investor. As Cohen observes, the character of property as power may be obscured by the premise that economic transactions are based on consent, e.g. the acquisition of land in the market; however, once control of resources is transferred, any owner—including a foreign investor—can dictate the use of the resources.<sup>26</sup> This can create a wide range of conflicts, which are governed by the applicable property laws. The central principle of these laws is that private property and the private use of the resources are not absolute. For states and local populations, retaining some control over the use of

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<sup>21</sup> See North, Douglas, *Structure and Change in Economic History* (New York: W. W. Norton, 1981), p. 21; Olstrom, Elinor and Edella Schlager, "The Formation of Property Rights," in Susan Hanna, Carl Folke and Karl-Göran Mäler (Eds.), *Rights to Nature: ecological, economic, cultural, and political principles of institutions for the environment* (Washington, D.C.: Island Press, 1996), p. 137.

<sup>22</sup> Stiglitz, Joseph, "Regulating Multinational Corporations: Towards Principles of Cross-Border Legal Framework in a Globalized World. Balancing Rights with Responsibilities," pp. 463-470.

<sup>23</sup> *Ibid.*, p. 470.

<sup>24</sup> Cohen, Morris, "Property and Sovereignty," *Cornell Law Quarterly* 13.8 (1927-1928), pp. 11-14.

<sup>25</sup> Hale, Robert, "Coercion and Distribution in a Supposedly Non-Coercive State," *Political Science Quarterly* 38.3 (1923), p. 471.

<sup>26</sup> Cohen, Morris, "Property and Sovereignty," p. 12



resources is central because the plans of the foreign investor can affect social life, the environment and the distribution of the benefits.

The environmental and social consequences of the use of resources are closely connected. Very often, the environment needs to be severely altered to make economic activities related to foreign investment like mining or large-scale agriculture possible. Such changes can have important social repercussions. The capital-intensive production of crops for instance will affect a local and independent group of peasants, who may be pushed to begin working as employees for the large undertakings. This project may create some well-paid jobs locally but it can also exacerbate overall poverty and inequality, worsening the living standards of the majority.<sup>27</sup>

The dominion granted by property can be consequently equated in many ways to the notion of sovereignty. The transfer of control over resources to foreign investors necessarily implies a cession of authority that goes beyond the mere development of particular projects. Barnet and Muller note that “in the course of their daily business [MNCs] make decisions with more impact on the lives of ordinary people than most generals and politicians.”<sup>28</sup> Local populations will predictably react when these decisions have negative consequences for them, urging host states to protect their interests and alternative views on the use of resources.<sup>29</sup>

What follows is that for domestic democracy to be consistent with foreign investors’ property rights, the principles of political determination and security of private property need to be balanced. There is no such thing as absolute property rights or absolute democracy, as Montesquieu and Madison already noted in the 18<sup>th</sup> century. The tension between private property and democracy is the most important topic in any constitutional property debate. For property defenders, private property promotes democracy as it allows individuals to exercise their autonomy, facilitating economic transactions. This view is promoted by the World Bank, for instance, that consistently relates private property with democracy and the rule of law.<sup>30</sup> This position, however, is in the best of the cases shortsighted. Realist and progressive scholars have clearly demonstrated that states and communities maintain an inherent interest in the use of the resources and the distribution of benefits, not because they do not want to respect individual property, but because the use of those resources can affect the individual autonomy of the non-

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<sup>27</sup> Perrone, Nicolás, “Restrictions to foreign acquisitions of agricultural land in Argentina and Brazil,” *Globalizations* 10.1 (2013): 205-209.

<sup>28</sup> Barnet, Richard and Ronald Muller, *Global Reach: The Power of the Multinational Corporations* (New York: Simon and Schuster, 1974), p. 214.

<sup>29</sup> See *TECMED v Mexico*, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003; and *Aguas del Tunari v Bolivia*, ICSID Case No. ARB/02/3.

<sup>30</sup> Waldron, Jeremy, *The rule of law and the measure of property* (Cambridge: Cambridge University Press, 2012).

owners and the community life.<sup>31</sup> Property is a political and relational concept that incorporates “ideas about ethics, justice, morality, or any other values and goals.”<sup>32</sup>

When describing the problems that private property in the hands of foreign investors create for sovereignty, democracy, and ultimately for local populations, it is necessary to consider the importance of the foreignness of the investor. This includes examining both foreign investors and home states. Historically, foreign investors have been identified with the national interest of their home states. In 1935, Staley described a world where “diplomacy serve[d] investments” and “investments serve[d] diplomacy.”<sup>33</sup> During the post-colonial context, MNCs were still considered agents of their home countries that served to maintain the economic dependency of the former colonies.<sup>34</sup> These corporations were a tool to consolidate a distribution of labour where developing countries produced natural resources and developed countries manufactured industrial goods. In reaction to this dominant view, many developing states decided to limit foreign investment in natural resources. A number of other countries implemented similar or even more stringent policies. During this period, Japan, South Korea and Finland remained quite closed to foreign investment, while France and Canada adopted measures concerned with the superiority of U.S. MNCs.<sup>35</sup>

Based on the policy changes in Canada, Bergsten in 1974 predicted “coming investment wars.”<sup>36</sup> In the following years, countries certainly struggled in relation to foreign investment, but the struggle was not so much for or against liberalisation but for the attraction of MNCs. In few years, foreign investment became very welcome and desired. The main reason for this shift was a rapid change of perception regarding multinational corporate activity. What in the 1960s and 1970s was considered problematic for development became by the end of the 1980s—hand in hand with neoliberalism—one of the essentials recipes for the very same goal.<sup>37</sup>

Part of this change arguably responded to the increasing detachment of MNCs from their home states. The world of global value chains and economic globalisation that Reich, and Stopford and Strange describe as a consolidated trend in the 1990s effectively contrasts with the

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<sup>31</sup> Alexander, Gregory, *The global debate over constitutional property: lessons for American takings jurisprudence* (Chicago: University of Chicago Press, 2006), pp. 1-7.

<sup>32</sup> Lehavi, Amnon, “The Global Law Of The Land,” *University of Colorado Law Review* 81 (2010), p. 469.

<sup>33</sup> Staley, Eugene, *War and The Private Investor: A Study in the Relations of International Politics and International Private Investment* (New York: Doubleday, Doran & Company, 1935), Chapters 3, 6.

<sup>34</sup> Gilpin, Robert, *Global political economy: understanding the international economic order* (Princeton, N.J.: Princeton University Press, 2001), pp. 286-288.

<sup>35</sup> Chang, Ha-Joon, “Regulation of foreign investment in historical perspective,” *The European Journal of Development Research* 16.3 (2004): 687-715; Servan-Schreiber, Jean, *The American challenge* (Harmondsworth: Penguin Books, 1969); Globerman, Steven and Daniel Shapiro, “The Impact of Government Policies on Foreign Direct Investment: The Canadian Experience,” *Journal of International Business Studies* 30 (1999): 513-532.

<sup>36</sup> Bergsten, Fred, “Coming investment wars?,” *Foreign Affairs* (1974): 135-152.

<sup>37</sup> Dunning, John and Sarianna Lundan, *Multinational enterprises and the global economy* (Cheltenham, UK; Northampton, MA: Edward Elgar, 2008), p. 675.

picture provided by Staley back in 1935.<sup>38</sup> This trend should not be exaggerated, however, because MNCs continue to be socially and culturally embedded in their home states.<sup>39</sup> What it is true is that the interests of these firms can presently diverge substantially from those of the home state. Today, multinational corporate plans transcend the nation-state and its interests, constituting “the first institution in human history dedicated to central planning on a world scale.”<sup>40</sup>

This change of perception on MNCs had implications for the regulation of foreign investment at the private property level. The fierce competition for foreign investment triggered a large number of regulatory changes. Most governments around the world unilaterally reversed many of the restrictive measures adopted in previous decades. UNCTAD data shows that 94% of the changes in foreign investment policies between 1992 and 2003 (1771 out of 1885) were liberalising and protective rather than restrictive.<sup>41</sup> The signature of investment treaties expanded at a rapid pace during this period, under the auspices of a “Grand Bargain” by which host states granted foreign investors international protection in exchange for the possibility to increase the inflow of capital.<sup>42</sup> As these neoliberal reforms were implemented, few governments paid attention to the warnings regarding the social and environmental risks involved with foreign investment.<sup>43</sup> The extensive authority granted to foreign investors according to the treaties—much of it in the form of strong property rights—was going to have profound effects for states and local populations, announcing the long series of disputes that twenty years later investment arbitrators are presently adjudicating.

### ***III. From multilateral disagreement to the BITs rush: Depolitisation or the politics of private property protection?***

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<sup>38</sup> Reich, Robert, *The Work of nations: preparing ourselves for 21st century capitalism* (New York: Vintage Books, 1992); Stopford, John and Susan Strange, *Rival states, rival firms: Competition for world market shares* (Cambridge: Cambridge University Press, 1991).

<sup>39</sup> Razeen, Sally, “Multinational enterprises, political economy and institutional theory: domestic embeddedness in the context of internationalization,” *Review of International Political Economy* 1 (1994): 161-192.

<sup>40</sup> Kobrin, Stephen, “Multinational Corporations, the Protest Movement, and the Future of Global Governance,” in Alfred Chandler Jr. and Bruce Mazlish (Eds.), *Leviathans: Multinational corporations and the new global history* (Cambridge: Cambridge University Press, 2005), p. 224.

<sup>41</sup> UNCTAD, *World Investment Report 2004: The Shift Towards Services* (New York and Geneva: United Nations, 2004), p. 8.

<sup>42</sup> Salacuse, Jeswald and Nicholas Sullivan, “Do BITs really work: An evaluation of bilateral investment treaties and their grand bargain,” *Harvard International Law Journal* 46 (2005): 67-130.

<sup>43</sup> See Lall, Sanjaya, “Multinational enterprises and developing countries: some issues for research in the 1990s,” *Millennium* 20.2 (1991): 251-255; Reich, Simon, “Roads to follow: regulating direct foreign investment,” *International Organization* 43.4 (1989): 543-584.

Historically, foreign investment has not been a peaceful domain. Investment disputes have led to expropriations, coup d'états and military interventions. Although only some foreign investment ends in turmoil, tensions between global corporate and local interests are latent and when the issues do escalate, they normally become political and difficult to resolve. No government wants to be seen accepting demands by foreign investors, in particular when at stake is a large land reform, the cultural industry or a historical reparation initiative, and they may rely on their sovereign powers to turn the situation in their favour. Foreign investors reasonably demand protection against this political risk, and in the event of a dispute would not hesitate to employ their economic power or to recur to their home states.

The large record of foreign investment disputes contrasts, interestingly, with the lack of international institutions in this field. If foreign investment disputes have been a concern for both developed and developing countries, the persistent multilateral disagreement and the inexistence of an international institution indicate how difficult it is to organise the governance of foreign investment. While developing countries have resisted some of the initiatives, which essentially aimed to protect foreign investment, other attempts in favour of a broader institutionalisation—such as the U.N. Code of Conduct on MNCs—were blocked by developed countries. On other occasions, developed countries at the OECD were unable to reach a consensus on their own terms.<sup>44</sup>

The list of disagreements begins in the 19<sup>th</sup> century with the Calvo Doctrine, according to which developing countries asserted that domestic laws govern foreign investment and eventual disputes should be decided before domestic courts. This position opposed the views of developed countries based on a doctrine firstly enunciated by Grotius and Vattel during the 16<sup>th</sup> and 17<sup>th</sup> centuries. In essence, the doctrine of diplomatic protection recognises an interest of home states over the property rights of their citizens in foreign countries, and this interest authorises home states to initiate legal proceedings at the international level and according to international law.

In the wake of the 20<sup>th</sup> century, the only international consensus was that countries should resolve foreign investment disputes peacefully. Home states were precluded to use force as long as host countries accepted to submit the dispute to international litigation (Drago-Porter Convention of 1907). The creation of the League of Nations did not imply any progress in this area. The only outcome of the conferences held at The Hague in 1930 was the confirmation of

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<sup>44</sup> Correa, Carlos and Nagesh Kumar *Protecting foreign investment: implications of a WTO regime and policy options* (New York: Palgrave, 2003), Chapter 3.

Newcombe, Andrew and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (The Netherlands: Kluwer Law International, 2009), Chapter 1.

the lack of consensus between developed and developing countries on most substantive issues.<sup>45</sup> Like most international economic topics, the matter was back on the agenda at the end of the Second World War. These negotiations were shaped by a positive view—mainly among developed nations—on the creation of international institutions to govern international trade, investment, finance and development. Trade and investment negotiations concluded with a draft of the Havana Treaty, whose main purpose was to create the International Trade Organisation. But as developed nations reached a consensus on trade with the conclusion of the General Agreement on Trade and Tariffs (GATT), foreign investment proved to be again controversial. The GATT had no disciplines on this area, and the United States rejected the Havana Treaty due to the opposition of the business lobby to the foreign investment chapter. The regulation of foreign investment was the only part of Bretton Woods project that came to nothing.<sup>46</sup>

The negotiations for a multilateral understanding on foreign investment did continue but only to suffer one failure after the other. Developing countries persisted in opposing most initiatives, while developed countries blocked any alternative project, and could not reach a consensus among themselves. In the 1960s, the Organisation of Economic Cooperation and Development (OECD) negotiated and approved the Draft Convention on the Protection of Foreign Property. Despite the common views of developed countries, some differences among OECD members impeded the signature of a multinational convention based on this draft.<sup>47</sup> In the meanwhile, developing countries pushed for an alternative model for foreign investment governance. Their objective was a regime that focuses less on protection and more on the problems that foreign investment can create for host countries and local populations. Developing countries channelled their voice through the United Nations, passing the resolutions on the Permanent Sovereignty over Natural Resources in 1962, and the Charter of Economic Rights and Duties of States in 1974. These resolutions were not binding—as every General Assembly resolution—and developed countries strongly objected to their content, in particular, to the Charter of Economic Rights.<sup>48</sup>

Foreign investment reappeared on the multilateral agenda during the Uruguay Round of the GATT. Again, despite the substantial consensus that led to the creation of the WTO, states did not reach any major consensus on foreign investment issues. The only exception was a relatively minor agreement on trade measures related to investments. After 1995, foreign investment

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<sup>45</sup> Borchard, Edwin, “Responsibility of States, at the Hague Codification Conference,” *The American Journal of International Law* 24.3 (1930): 517-540.

<sup>46</sup> Dattu, Riyaz, “A Journey from Havana to Paris: The Fifty-Year Quest for the Elusive Multilateral Agreement on Investment,” *Fordham International Law Journal* 24.1 (2000), pp. 286-288.

<sup>47</sup> Newcombe, Andrew and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment*, p. 30.

<sup>48</sup> *Ibid.*, pp. 31-33.

remained on the agenda of the WTO only for a short period. It was discussed during the Doha Development Road, but abandoned at the Cancun Ministerial Meeting in 2003.<sup>49</sup> In the meantime, developed countries tried to reach a consensus of their own within the framework of the OECD. This strategy followed the premise that the disagreement on foreign investment is a *North v South* debate. Yet, as had already happened in the 1960s, some developed countries opposed to the conclusion of the Multilateral Investment Agreement (MIA) in a scenario of rising civil society pressure due to the potential risks that this initiative posed to environmental protection.<sup>50</sup>

This systematic lack of consensus, despite the importance of the problem, is explicable when the focus of foreign investment rules has been placed on facilitating multinational corporate activity and obstructing change in host countries. In other words, this lack of consensus makes sense if we think about these rules as property rules. The resistance of Latin American countries was not only a question of preserving sovereignty in the abstract. In 1968, Metzger noted that the views of Mexico during the land reform of the early 20<sup>th</sup> century were understandable given that foreign investment rules constituted an obstacle to change, which amounted to a total barrier “if foreign investors were dominant.”<sup>51</sup> The situation is not so different when we move to developed countries. French and Canadian resistance to the application of the MIA to their cultural industry is based on a similar concern. This industry works under premises that are different from those of the main MNCs in this sector, and these countries are aware that facilitating the activity of the latter could eventually affect the premises that support their cultural industry. Once MNCs become dominant, there will not be a space to change. As Schneiderman has recently put it, “[a] pluralistic understanding of civilisations would be buried beneath the weight of [this] international law project.”<sup>52</sup>

Until the 1990s, in any case, foreign investment disputes remained governed by contracts and general international law. A review of the literature between the 1960s-1980s demonstrates that most foreign investment disputes were resolved through contractual means, i.e. arbitrations contracts, and according to general international law.<sup>53</sup> This does not mean that during this period there were no international developments in the governance of foreign investment.

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<sup>49</sup> Smythe, Elizabeth, “Just Say No!: The Negotiation of Investment Rules at the WTO,” *International Journal of Political Economy* 33.4 (2003): 60-83.

<sup>50</sup> Dattu, Riyaz, “A Journey from Havana to Paris: The Fifty-Year Quest for the Elusive Multilateral Agreement on Investment,” pp. 299-300.

<sup>51</sup> Metzger, Stanley, “Private Foreign Investment and International Organizations,” *International Organization* 22 (1968), p. 291.

<sup>52</sup> Schneiderman, David, “The Global Regime of Investor Rights: Return to the Standards of Civilised Justice?,” *Transnational Legal Theory* 5.1 (2014), p. 62.

<sup>53</sup> Yackee, Jason, “Pacta Sunt Servanda and State Promises to Foreign Investors before Bilateral Investment Treaties: Myth and Reality,” *Fordham International Law Journal* 32:5 (2008), pp. 1569-1596.

Beginning in 1959, many European countries signed BITs with former colonies, inaugurating a trend that continued throughout the 1960s and 1970s. In addition, the World Bank sponsored the negotiation of the Convention for the creation of the International Centre for the Settlement of Investment Disputes in (ICSID), which was finally approved by the minimum number of countries in 1966, despite the opposition of Latin American countries.

But both BITs and the ICSID remained dormant for 30 years. At the beginning of the 1980s, there were less than 250 BITs and only 9 registered disputes registered at the ICSID. The main foreign investment disputes of that time, involving countries such as Libya, Kuwait and Iran, were resolved outside of ICSID and according to general international law. This picture completely changed during the 1990s. In the period 1994-1996, states were signing an average of 4 BITs per week. Today, the amount of bilateral, regional and sector-specific investment treaties exceeds 3,000. The caseload of the ICSID reflects this boom. In 1997, the number of cases registered per year had reached 10, and since 2000, the annual average has remained well above 20 (50 in 2012). Most controversial disputes of this period, involving countries such as Argentina, Ecuador and Venezuela, have been resolved within the IIR, i.e. through investment arbitration and according to investment treaties.<sup>54</sup>

This scenario led some authors in the middle of the 2000s to argue that most states had reached a kind of *de facto* multilateral consensus on foreign investment.<sup>55</sup> It is indisputable that during a brief period many states literally rushed to sign treaties with as many countries as possible. There is some evidence, however, that many states were not fully aware of the legal consequences of those treaties.<sup>56</sup> Rather than a consensus on the content of the IIR, then, the signature of the treaties reflects the foreign investment rush of the 1990s and the dominance of neoliberal ideas. The Grande Bargain of protection for foreign investment was highly embedded in the Washington consensus, which promoted private property protection as a central part of a one size fits all development approach. But the Washington consensus did not do very well in the field of foreign investment. Many studies have shown that BITs do not increase foreign investment flows or have at best only limited effects, while the relationship between these flows and development is unclear.<sup>57</sup> If there ever was a *de facto* multilateral consensus, it was a very brief one.

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<sup>54</sup> According to UNCTAD and ICSID statistics.

<sup>55</sup> Schill, Stephan, *The Multilateralization of International Investment Law* (New York: Cambridge University Press, 2009).

<sup>56</sup> Poulsen, Lauge, *Sacrificing sovereignty by chance: investment treaties, developing countries, and bounded rationality*, Diss. London School of Economics and Political Science (LSE), 2011.

<sup>57</sup> UNCTAD, *The Role of International Investment Agreements in Attracting Foreign Direct Investment to Developing Countries*, (New York and Geneva: United Nations, 2009); Sumner, Andrew, "Is foreign direct investment good for the poor? A review and stocktake," *Development in Practice* 15:3-4 (2005), pp. 281, 269-285.

In addition, as some scholars had warned, the retreat of the state in the regulation of foreign investment quickly translated into increasing disputes and discontent in host countries and local populations. The rise of neoliberalism brought about increasing criticism against international economic institutions across the board. The WTO, the IMF and the World Bank were under strong pressure in the late 1990s and early 2000s, although they have managed to overcome much of the legitimacy crisis by now. The situation of the IIR is slightly different because this regime has been by far and large the most criticised in the recent years, and there remains considerable resistance to its present structure and expansion.

The denunciation of ICSID by Venezuela, Bolivia and Ecuador are important indicators of the relevance of this criticism, as are the decisions of Australia, the Czech Republic, South Africa and recently Indonesia to modify, denounce or stop signing investment treaties.<sup>58</sup> This criticism does not indicate a decay of the IIR, however, because some level of resistance is inherent to the political game. But what is different about the current crisis in the IIR is the increasing criticism in developed countries after these states have become subject to a few investment arbitrations. In other words, it was to be expected to see Ecuador or Venezuela criticising the effects of investment treaties, after all they are the others, but it is certainly a new development to see Europe and particularly Germany resisting the inclusion of an investment chapter in the Transatlantic Agreement.<sup>59</sup> This attitude of developed countries could be a signal of a large change of circumstances because investment treaties allegedly incorporate the preferences of these countries.

In this regard, current developments in investment treaty making show some of the main proponents of investment treaties and arbitration slightly shifting their discourse towards the IIR, trying to reconstitute its original asymmetric structure. This strategy aims to reverse the universalisation of the IIR in a move that would equal to making the GATT applicable to 'other' countries only.

There is substantial evidence of this strategy. First, the only FTA the United States have signed in recent years without an investment chapter was with Australia. The explicit reason for this decision was that countries with developed and trustworthy legal systems did not need investment arbitration.<sup>60</sup> Second, the existing debate in the European Union shows that

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<sup>58</sup> UNCTAD, "International Investment Policy Making in Transition: Challenges and Opportunities of Treaty Renewal," IIA Issues Note 4, June 2013; Bland, Ben and Shawn Donnan, "Indonesia to terminate more than 60 bilateral investment treaties," *Financial Times*, March 26, 2014.

<sup>59</sup> Donnan, Shawn and Stefan Wagstyl, "Transatlantic trade talks hit German snag," *Financial Times*, March 14, 2014.

<sup>60</sup> Dodge, William, "Investor-state dispute settlement between developed countries: reflections on the Australia-United States Free Trade Agreement," *Vanderbilt Journal of Transnational Law* 39 (2006): 1-37.



according to the Commission and some member states such a regime is not needed within Europe. The incorporation of the Eastern European countries implies their adherence to acceptable principles of law.<sup>61</sup> Third, the inclusion of an investment chapter in the future Transatlantic Agreement is gaining new and new detractors. These are not the usual suspects only, such as environmental NGOs or the government of France. They include, for instance, the libertarian CATO Institute.<sup>62</sup> The philosophy behind this ‘change of mind’ is summarised well in one of the latest documents issues by UNCTAD:

In that context, questions arise about the rationale for including ISDS [investment arbitration] into IIAs—or other agreements—between developed countries with sophisticated regulatory and legal systems, and with generally open investment environments. Originally, the primary purpose of IIAs was the provision of legal protection to foreign investors, including through ISDS [investment arbitration], hence addressing concerns that host countries’ domestic legal systems may not be advanced enough to ensure due process, fair and non discriminatory treatment and adequate compensation for expropriation.<sup>63</sup>

The position of the EU and some key U.S. actors carry a great deal of either inconsistency or hypocrisy.<sup>64</sup> If these countries want the IIR to consolidate as a way to favour their MNCs, why do they resist the incorporation of investment arbitration in their own economic treaties? In theory, they should have nothing to fear. A leading arbitrator affirmed in a lecture at Georgetown in 2005 that the only objective of the IIR is to discipline host states that do not comply with their commitments and the rule of law.<sup>65</sup> To a great extent, this message has been repeated in most investment awards. No tribunal claims to be affecting host state legitimate authority to regulate.<sup>66</sup> Assuming that the EU is aware of the negative consequences their position may have on the future of the IIR, it is worth reflecting about the reasons behind the

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<sup>61</sup> Tietje, Christian, “Bilateral Investment Treaties Between EU Member States (Intra-EU-Bits) - Challenges in the Multilevel System of Law,” *Transnational Dispute Management* 10.2 (2013).

<sup>62</sup> Ikenson, Daniel, “A Compromise to Advance the Trade Agenda: Purge Negotiations of Investor-State Dispute Settlement,” CATO Institute, *Free Trade Bulletin* 57 (2014).

<sup>63</sup> UNCTAD, “Recent Developments in Investor-State Dispute Settlement (ISDS),” p. 25.

<sup>64</sup> See the presentation of Lord Goldsmith at the European Union Committee of the House of Lords, 14th Report of Session 2013–14, para. 159.

<sup>65</sup> Paulsson, Jan, “The Power of States to Make Meaningful Promises to Foreigners,” *Journal of International Dispute Settlement* 1.2 (2010): 341 - 352. See also [http://legal.un.org/avl/ls/Paulsson\\_IEL.html](http://legal.un.org/avl/ls/Paulsson_IEL.html).

<sup>66</sup> See among others *TECMED v Mexico*, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003, at 119; *MTD v Chile*, ICSID Case No. ARB/01/7, Award, 25 May 2004, at 98; *Suez and others v Argentina*, ICSID Case No. ARB/03/17, Decision on Liability, 30 July 2010, at 139.

opposition of some of its members regarding investment arbitration in the negotiations of a Transatlantic Agreement.

More than a question of paying compensation to a particular investor, I claim that what populations in developed (and developing countries) fear is that MNCs can use investment arbitration to impose their views on the use of resources, defeating their democracies and any possibility of pluralism. Their fear then is the ‘depolitisation’ of private property. Many authors have emphasised that the main strength of the IIR is precisely its depolitisation. Before, the field of foreign investment disputes was the domain of diplomatic relations, political intervention, and state-to-state dispute settlement. This position is not without merit. A problem faced by MNCs in the 1960s and 1970s was the allegation that they were agents of home states, and obviously the fact that any dispute with the host state could end up in a diplomatic intervention only validating this allegation. The IIR resolves this problem by giving foreign investors direct standing at the international level. Similarly, investment arbitration has been defended by small countries because it helps them to prevent foreign interference in domestic affairs. After the establishment of an investment arbitration, domestic authorities can always answer a powerful country as the United States that the issue has been deferred to an allegedly independent and impartial international tribunal.<sup>67</sup>

The problem of this argument is not that investment arbitration has not reduced state authority and intervention in foreign investment protection —to this extent, the depolitisation argument is not inaccurate. The problem is that this definition of politics and depolitisation is very unsatisfactory and it does not capture the essential political character of any regime that governs the use of resources. Needless to say, the relational implications of property extend well beyond the participation of the state in the protection of private property.

Against this background, I propose to analyse the governance implications of the IIR using the lens of privatisation. By privatisation of foreign investment governance, I am referring to something broader than foreign investors’ international standing and the lower participation of home states. Privatisation implies the emergence of a regime that privileges the position of MNCs, and relies on their expectations on the uses and benefits of resources to discipline host states. Three characteristics of the IIR support this claim of privatisation. International arbitration, i.e. litigation and not political cooperation, is the central and only institutional mechanism of the IIR; foreign investment disputes are resolved from an individual micro-

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<sup>67</sup> See Paparinskis, Martins, “The Limits of Depolitisation in Contemporary Investor-State Arbitration,” *Select Proceedings of the European Society of International Law* 3 (2010).

perspective that focuses only on property protection; the IIR increases foreign investors' and arbitrators' authority *vis-à-vis* host and home states.

First, the IIR is a highly legalised regime where political representation and cooperation is absent. In institutional terms, the only solution that this regime provides is litigation, and this litigation has remained thus far limited to claims initiated by foreign investors. This means that the main input of the legal proceedings always comes from MNCs. Such a model shares most in common with a new medieval type of governance because the political role of states is quite modest, being limited to the negotiation or renegotiation of treaties.<sup>68</sup> Second, the IIR focuses essentially on the protection of foreign investors' rights, whereas the impact of foreign investment on the community has been left to domestic legal orders. Given the prevalence of international over domestic law, this ends up benefiting foreign investors' perspective on the conflict. This perspective is also favoured by the inter-partes model of adjudication followed by most investment arbitration. Investment arbitration borrows from commercial arbitration an individual micro-perspective on the disputes.<sup>69</sup> Third, investment arbitration operates as a transnational tribunal. Arbitrators are more autonomous from governments and more dependent on foreign investors because they rely on the latter to exercise their jurisdiction. This leads Tai-Cheng to conclude that investment arbitration implies a strong redistribution of power from states to foreign investors and investment arbitrators.<sup>70</sup> Such redistribution is significant because investment treaties deal with incomplete foreign investors' rights and mainly incorporate vague and ambiguous protective standards, increasing the scope of arbitral interpretation.

It could be argued that empowering investment arbitrators is a positive move for the fair decision of foreign investment disputes. Arbitrators are in theory appointed because of their independence and impartiality. There are rules in the ICSID that prevent nationals to sit in cases where an investor or a state of her nationality is involved. However, a closer look at the situation of investment arbitrators shows that there are significant problems with the independence and impartiality of arbitrators. First, investment arbitrators have a group interest in the future of investment arbitration, and an individual interest in their prospect of future appointments. The outcome of the arbitrations, to this extent, is not neutral to their interests particularly at the

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<sup>68</sup> Slaughter, Anne-Marie, "The real new world order," *Foreign Affairs* 76 (1997), pp. 183-184, 195-197.

<sup>69</sup> DiMascio, Nicholas and Joost Pauwelyn, "Nondiscrimination in Trade and Investment Treaties: Worlds Apart or Two Sides of the Same Coin?," *The American Journal of International Law* 102 (2008), p. 54-56; Hirsch, Moshe, "The Sociology of International Investment Law," in Zachary Douglas et al. (Eds.), *The Foundations of International Investment Law: Bringing Theory into Practice* (New York: Oxford University Press, 2014): 143-167; *Glamis Gold v United States*, NAFTA – UNCITRAL, Award, 8 June 2009, at 3, 7.

<sup>70</sup> Cheng, Tai-Heng, "Power, Authority and International Investment Law," *American University International Law Review* 20.3 (2005), pp. 481, 492.

jurisdictional stage.<sup>71</sup> Second, they belong to an international community that has been historically involved with the business side of the struggle. International lawyers have promoted investment treaties both in the 1960s and in the 1990s.<sup>72</sup> More importantly, the main problem of investment arbitrators is that their discourse of technical correctness is not consistent with their function of resolving property disputes. Decisions regarding private property protection, especially in relation to state intervention, are not the outcome of independent technical assessments but of normative preferences. Arbitrators cannot be technically correct only because the meaning of property is plural and depends on the normative arguments they are convinced by.<sup>73</sup>

All in all, the alleged depolitisation of the IIR in reality hides a political message in favour of the protection of foreign investors' private property. In normative terms, the IIR is justified because foreign investment protection can lead to the most efficient use of resources, and this would eventually improve the living standards of the population.<sup>74</sup> But this casual relationship is far from clear, and investment arbitration ends up being solely an instrument that MNCs can use to monitor and discipline host state behaviour. Foreign investors can rely on investment arbitration to punish any "irrational nationalism" affecting global planning and the expected profits.<sup>75</sup> On the losing side of this regime, inexorably, we find local populations and alternative views on the use of resources. In this respect, the evidence shows that investment arbitrators may decide disputes in ways different from domestic courts, and this includes the courts of developed legal systems.<sup>76</sup>

#### ***IV. A way forward: Governing foreign investment through a political institutional structure***

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<sup>71</sup> McArthur, Kathleen, and Pablo Ormachea, "International Investor-State Arbitration: An Empirical Analysis of ICSID Decision on Jurisdiction," *Review of Litigation* 28 (2008): 559-594; Van Harten, Gus, *Investment treaty arbitration and public law* (New York: Oxford University Press, 2007).

<sup>72</sup> *Ibid.*; Schwarzenberger, Georg, "The Abs-Shawcross Draft Convention on Investments Abroad: A Critical Commentary," *Journal of Public Law* 9 (1960), p. 148.

<sup>73</sup> Waldron, Jeremy, *The right to private property* (Oxford: Clarendon Press, 1988), p. 433; Ackerman, Bruce, *Private Property and the Constitution* (New Haven and London: Yale University Press, 1977), p. 29.

<sup>74</sup> See the preambles of US Investment treaties, available at <http://www.bilaterals.org/?-us-bits->.

<sup>75</sup> Kobrin, Stephen, "Multinational Corporations, the Protest Movement, and the Future of Global Governance," p. 225.

<sup>76</sup> See Van Harten, Gus, *Investment treaty arbitration and public law*; Schneiderman, David, *Constitutionalizing Economic Globalization. Investment Rules and Democracy's Promise*.

In 2003, Mann claimed that the IIR is at a crossroad: it can crystallise as a new form of colonialism or it can evolve into a new field of global cooperation on development.<sup>77</sup> Today, many academic circles share the view that the IIR is in need of a change, with proposals ranging from the negotiation of a multilateral investment agreement to the recognition of a larger role for state-to-state arbitration.<sup>78</sup> This recent literature, however, neither refers to the rationale that justifies implementing any of these particular initiatives, nor explains why formulas that failed in the past will work in the present. Arguably, the starting point for resolving the governance problem of foreign investment should be the political economy of the problem, and not the multilateralisation of the existing regime or the sound interpretation of the law — something that is in itself difficult to determine. Foreign investment creates a series of challenges regarding the use of resources, and can have large social, cultural and environmental implications. These are political issues whose resolution requires politics and cooperation. In this regard, the literature referred to overlooks that global governance in a plural world cannot be achieved through litigation only; investment arbitration is simply not enough.

Increasing the role of politics in the governance of foreign investment requires the creation of political institutions rather than the improvement of dispute resolution mechanisms. Investment arbitration cannot create consensus, it can only determine winners and losers. Tribunals, in addition, require long periods of time to adapt to new normative views about the subject in question. What the governance of foreign investment needs thus is more space for negotiation and cooperation, and less litigation, whether it is investor-state or state-to-state. The IIR shows that too much legalisation and too little politics is a recipe to increase tensions. Political institutions, on the other hand, can narrow down the gaps between winners and losers, and can be reworked more easily to cope with emerging tensions. Political bodies can react faster because they have a macro-perspective on the situation.<sup>79</sup>

To increase the role of politics in the governance of foreign investment, it is necessary to put the emphasis on the existing institutions along the lines argued by the late Rawls.<sup>80</sup> They need to be reorganised as a way to promote consensus among the different actors involved, and not as a means to favour some self or group-interests. The first step to promote politics is to open up institutions to dialogue and democratic decision-making. The governance of foreign investment

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<sup>77</sup> Mann, Howard “ International Investment Agreements: Building the New Colonialism?” *American Society of International Law Proceedings* 97 (2003), p. 247.

<sup>78</sup> See above n 15.

<sup>79</sup> Freitag, Markus and Marc Bühlmann, “Crafting Trust: The Role of Political Institutions in a Comparative Perspective,” *Comparative Political Studies* 42.12 (2009), p. 1546-7; Immergut, Ellen, “The theoretical core of the new institutionalism,” *Politics and Society* 26 (1998), p. 9.

<sup>80</sup> Rawls, John, “The Idea of an Overlapping Consensus,” *Oxford Journal of Legal Studies* 7 (1987): 1-25.

needs a transformation that can be briefly summarised as the opposite of the legalisation of the GATT. The difficulty with the governance of international trade in the 1980s was the excessive politicization of the GATT. On the contrary, the present problem of the IIR is its excessive legalisation. It has plenty of the ethos of lawyers and arbitrators but misses the ethos of diplomats and politics more in general.<sup>81</sup> This is a cornerstone for higher levels of general trust in the governance of international economic affairs.<sup>82</sup>

The creation of this international political structure obviously faces the existing difficulties to reach a multilateral consensus on foreign investment. But it is necessary to distinguish here between the obstacles to reach a substantive multilateral consensus on the use of the resources by MNCs and the difficulties to establish a political forum to discuss and decide policy approaches to the challenges posed by MNCs and foreign investment. As Rawls explains, reaching an overlapping consensus on significant normative issues is quite difficult domestically, let alone internationally. He argues, however, that an overlapping consensus on the institutional mechanisms to accommodate conflicting interests is possible.<sup>83</sup> In the case of foreign investment governance, it becomes almost an imperative. Property is a highly plural concept that enables and shapes community life.<sup>84</sup> Plural views about property put pressure on the institutions aimed to govern foreign investment and, the more plurality of values, the stronger the need for political institutions.

This line of reasoning could favour the inclusion of foreign investment governance in the WTO. This organisation arguably represents a political consensus on the institutional structure to govern international trade. But the WTO faces its own challenges today. The difficulties of the Doha Round reveal that the members have diverging views about the purpose of this organisation and the future of international trade. In this context, introducing the governance of foreign investment in the WTO may be a mistake not only because of the impracticality of negotiating such a reform, but also because of the challenges that the institutionalisation of foreign investment will create.

In this regard, there are two central differences between the WTO and the IIR. First, as opposed to what happens in the WTO, MNCs have an active role in the IIR. This could change in the future but making the institutionalisation of foreign investment governance conditional to

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<sup>81</sup> Weiler, Joseph, "The Rule of Lawyers and the Ethos of Diplomats Reflections on the Internal and External Legitimacy of WTO Dispute Settlement," *Journal of World Trade* 35.2 (2001): 191-207;

<sup>82</sup> See Howse, Robert, "From Politics to Technocracy-and Back Again: The Fate of the Multilateral Trading Regime," *The American Journal of International Law* 96.1 (2002), p. 97-98.

<sup>83</sup> Rawls, John. "The Idea of an Overlapping Consensus," pp. 4-5.

<sup>84</sup> Alexander, Gregory, Eduardo Peñalver, Joseph Singer and Laura Underkuffler, "A Statement of Progressive Property," *Cornell Law Review* 94 (2009), pp. 743-744.

such change is not necessary and perhaps not desirable. The recognition of MNCs as subjects of international law is not only a matter of rights but also of obligations. Second, the IIR may be a regime with some multilateral characteristics, but contrary to the WTO, it is composed by a large number of bilateral and regional treaties. An international organisation dedicated to the governance of foreign investment will need to administer this entire network of treaties. This is arguably possible because of the enormous similarities between the text of the treaties and the operation of the MFN clause. However, it is a challenge, and one unique to the governance of foreign investment.

But the main challenge posed by the institutionalisation of foreign investment governance is arguably finding the right balance between the to be created political bodies and investment arbitration. The inclusion of more politics clearly does not imply the end of disputes, and thus it is necessary to consider which institutional structure would promote the best possible relation between the political and dispute resolution bodies. First of all, the dispute resolution mechanism should aim to concentrate all foreign investment disputes. The present dispersion of arbitration forums responds more to the medieval reality of commercial arbitration than to the global need to govern foreign investment. This requires some reorganisation, in particular merging the ICSID into the new international organisation. In itself, this would represent a salutary move in terms of legitimacy because the voting system of the World Bank is still shaped by the same power relations that determined the asymmetric structure of the IIR. In addition, the creation of an appellate body makes more sense in this institutional context, as it would facilitate the dialogue between the political and jurisdictional bodies in charge of governing foreign investment.

Gathering the political and dispute resolution bodies in charge of foreign investment under the same institutional scope is just the starting point of the institutional challenge. As the WTO literature shows, the difficult part is to establish the relation between these two different bodies.<sup>85</sup> The political bodies should discuss issues that are of interest to all the members, remaining neutral regarding ongoing investment disputes. By now it is clear that developed and developing states face similar challenges in investment arbitration. The arbitrations faced by Argentina due to its economic crisis are now repeating again in Greece, Spain and Cyprus. Countries as different as Uruguay and Australia are defending themselves against similar claims from Philip Morris. And the tensions between international investment law, environmental law and human

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<sup>85</sup> Roessler, Frieder, "The Institutional Balance Between the Judicial and Political Organs of the WTO," in Marco Bronckers and Reinhard Quick (Eds.) *New Directions in International Economic Law. Essays in Honour of John H. Jackson* (The Hague; Boston: Kluwer Law International, 2000), p. 325; Bartels, Lorand, "The Separation of Powers in The WTO: How To Avoid Judicial Activism," *International and Comparative Law Quarterly* 53 (2004): 861-895.

rights law are always latent, no matter whether the dispute is against a developed or a developing country. Arguably, these issues would be better treated at a macro and political level, rather than from a ‘depoliticised’ micro-perspective angle. Drawing from the experience of the WTO, the political bodies of an international organisation in charge of foreign investment governance could create committees on foreign investment and the environment, foreign investment and human rights, and foreign investment and development.

The purpose of these discussions should not be to annul the obligations assumed in investment treaties but rather to help investment arbitrators to interpret the vague and ambiguous terms of the treaties. The Appellate Body of the WTO has accepted the significance of several acts of the political bodies for the resolution of concrete disputes. They include the creation of a Committee on Trade and Environment,<sup>86</sup> the deliberations of the Committee on Balance of Payments,<sup>87</sup> and the decisions of the Committee on Phytosanitary Measures.<sup>88</sup> In fact, the Appellate Body has rarely ignored the opinions of the political bodies of the WTO — sometimes even to the detriment of progressive goals.<sup>89</sup> Following the WTO practice, in addition, a political structure for the governance of foreign investment should entitle states to make comments on investment awards, inform an eventual appellate body about their concerns, and even have the ability to overturn an award by consensus, i.e. the rule of negative consensus.

The introduction of politics in foreign investment governance entails both opportunities and risks for non-state actors. A political structure would benefit civil society and NGOs, facilitating their coordination and action.<sup>90</sup> Presently, NGOs can only lobby governments regarding whether to sign or reject new investment treaties. The rest of their activities are dispersed among different tribunals that are treating similar issues. For the international business lobby, this cannot be seen as a negative development either, because it can certainly organise itself around any new institutional structure. The outcome would therefore be more plurality of voices in a political— as opposed to a jurisdictional—environment.

The risks posed by the institutionalisation of foreign investment governance are the excessive politicisation of the field and the potential lack of independence of investment arbitrators. This would be the main concern for foreign investors, and the arbitration and academic community

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<sup>86</sup> WTO Appellate Body Report *United States — Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 12 October 1998, para 154-155.

<sup>87</sup> WTO Appellate Body Report *India — Quantitative Restrictions*, WT/DS90/AB/R, adopted 22 September 1999, para. 103.

<sup>88</sup> WTO Panel Report *United States — Certain Measures Affecting Imports of Poultry from China*, WT/DS392/R, adopted 29 September 2010, para 7.134-7.136.

<sup>89</sup> Bartels, Lorand, “The Separation of Powers in The WTO: How To Avoid Judicial Activism,” p. 861.

<sup>90</sup> Tarrow, Sidney, “Transnational politics: contention and institutions in international politics,” *Annual Review of Political Science* 4.1 (2001): 1-20.



should remain vigilant in this respect. But I suggest that these risks are much lower in the foreign investment than in the trade field. As opposed to what happens in trade, many investment arbitrators are high profile international lawyers and academics. Arguably, these individuals will be much less prone to accept institutional pressure. There is indeed evidence of the strong attitude taken by an arbitrator when he received suggestions from the ICSID Secretariat.<sup>91</sup>

## ***V. Conclusion***

That the use and benefit of resources is a central issue of governance at both the domestic and international level does not strike anybody as contentious. What may seem controversial is that the IIR deals with the control of resources of different countries. For many decades, the literature has described the IIR as a regime solely aimed to protect foreign investors' rights. But this description is incomplete. The IIR has a direct impact on foreign investors, host states and local communities in relation to the use and benefit of resources. From this perspective, those who promoted the creation of a broad institutional structure to govern foreign investment and MNCs were taking a reasonable path in light of the political economy of the problem. They may have failed to realise some of the obstacles to reach such goal, but they were right in asserting that MNCs were only going to promote general welfare if there was an international regime in place able to strike a balance between multinational corporations, states and local populations.

The IIR however is not capable of taking politics seriously. This article has shown that rather than opening up a political space for discussing the implications of foreign investment, international arbitration only advances the protection of foreign investors' rights. The IIR puts host states and local populations in a situation of vulnerability *vis-à-vis* foreign investors. This purpose made sense to developed countries as long as this regime was only applicable to others. But as the asymmetric character of the IIR fades, the resistance to the universalisation of this regime is becoming generalised too. While developing countries want to abandon or limit the negative consequences of the IIR, developed countries want to support this regime but—as in the past—only for others.

The current resistance to the IIR opens up a space for imagining alternative regimes to govern foreign investment and MNCs. As opposed to the existing IIR, a broader institutional structure could constitute the basis for considering the plurality of interests and values involved in the use of resources by MNCs. This should arguably be the purpose of any international regime in this

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<sup>91</sup> See Additional Opinion of Professor Jan H. Dalhuisen in *Compañía de Aguas del Aconquija S.A. and Vivendi Universal S.A. v Argentina*, ICSID Case No. ARB/97/3, Second Annulment Proceeding of 17 December 2007.

field. The institutionalisation of foreign investment governance is certainly not the panacea, and the WTO is an example of the kind of problems that lie ahead. The creation of political bodies, in this respect, should only be seen as an adequate means to promote cooperation and trust among nations in relation to foreign investment. The path to make foreign investment serve divergent national interests better is a long and difficult one. It certainly includes, for instance, the attempt of some countries to recover their privileged status in the present regime. But we should not forget that the moment of highest consensus of the trade system—as Dunoff notes—was before the WTO, when the diplomatic ethos dominated the GATT.<sup>92</sup> After all, consensus is the business of politics.

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<sup>92</sup> Dunoff, Jeffrey, “The Politics of International Constitutions: The Curious Case of the World Trade Organization,” in Jeffrey Dunoff and Joel Trachtman, *Ruling the world?: constitutionalism, international law, and global governance* (New York : Cambridge University Press, 2009), pp. 195-196.

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